

STAFF REQUEST FOR PERMISSION TO PROCEED WITH A PUBLIC MEETING TO  
DISCUSS A POSSIBLE ADDITION TO REGULATION 25120 TO PROVIDE  
A DEFINITION OF GROSS RECEIPTS

Staff requests Board approval to schedule a public meeting to discuss the possible addition of a regulation under the Uniform Division of Income for Tax Purposes Act ("UDITPA"), Revenue and Taxation Code sections 25120 through 25139, defining the term "gross receipts." Under current law the term "gross receipts," which is the operative term in the definition of "sales" under UDITPA, is not defined in either UDITPA or the regulations implementing its provisions. The consistent determination of items that should or should not be included as gross receipts under the provisions of UDITPA is important to the uniform application of the sales factor of the California apportionment formula under UDITPA.

For example, many corporations invest idle cash in short-term financial instruments in order to maximize their income. Because the cash needs of a business may vary substantially from day to day, these investments usually consist of highly liquid assets that frequently mature in very short periods of time, often no more than several days, and in many cases, overnight. Typically, these instruments are held to maturity. In such circumstances, a question arises as to whether a portion of the cash that a corporation receives upon the maturity of an instrument represents the return of capital, and thus, whether or not it is a receipt that should be properly included in the sales factor.

The department is currently defending six suits for refund involving the proper sales factor treatment of investments of idle cash in short-term financial instruments held to maturity. One of the defenses the department has asserted in these cases is that holding these instruments to maturity results in a return of capital to the taxpayer that does not constitute a receipt for sales factor purposes. In the two cases where this defense has been ruled upon by trial courts, the department's position has been sustained, and the taxpayers have or are expected to file an appeal.

Additional questions have arisen with respect to the proper sales factor treatment of amounts received from other transactions, such as proceeds received as a result of litigation or forgiveness of indebtedness. The issue of the proper sales factor treatment of a litigation award is currently pending before the State Board of Equalization in the *Appeal of Polaroid Corporation*.

The Multistate Tax Commission has adopted Model Regulation IV.2.(a) defining the term "gross receipts." This model regulation may serve as one potential approach to defining gross receipts under UDITPA. Adopting a regulation defining gross receipts would provide needed guidance to the taxpaying community and the department's staff, as well as fostering uniformity among apportioning states.

A proposal to amend Regulation 25120 based upon the MTC proposal was submitted by staff on the department's proposed rule-making calendar for 1999. At the August 6,

1998, meeting of the Franchise Tax Board, members Connell and Andal directed staff to abandon this proposed regulation project. This proposal has not been the subject of a symposium. The possible adoption of a regulation addressing the definition of gross receipts was included in the staff's proposed rule-making calendar for the year 2003. At the Board meeting of November 26, 2002, the Board unanimously approved the rule-making calendar as proposed by staff for 2003 "with the exception of items previously rejected by the Board." The language of that Board action would appear to apply to a possible amendment to Regulation 25120.